FISCAL NOTE

Bill #:	HB0569	**Title:**	Clarify classification and valuation of oil and gas pipelines
Primary Sponsor:	McNutt, W	**Status:**	As Introduced - Revised

Sponsor signature Date David Ewer, Budget Director Date

Fiscal Summary

	FY 2006 **Difference**	FY 2007 **Difference**
Expenditures:		
General Fund	$102,622	$0
Revenue:		
General Fund	($286,383)	($286,325)
State Special Revenue	($17,987)	($17,983)
Net Impact on General Fund Balance:	($389,005)	($286,325)

- ☒ Significant Local Gov. Impact
- ☐ Included in the Executive Budget
- ☐ Dedicated Revenue Form Attached
- ☒ Technical Concerns
- ☒ Significant Long-Term Impacts
- ☐ Needs to be included in HB 2

Fiscal Analysis

ASSUMPTIONS:

Department of Revenue (DOR)

1. HB 569 specifies that all oil and gas production property of a "producer" is not centrally assessed property. A producer is defined as a legal entity that is liable for oil and gas production taxes under Title 15, Chapter 36 MCA. (See technical notes)
2. Under current law, oil and gas production property is classified as centrally assessed class 9 property and has a tax rate of 12%. Under the proposal, oil and gas production property of a "producer" would no longer be classified as class 9 property, but would now be locally assessed as class 8 property with a tax rate of 3%.

Reclassification of oil and gas production property of producers

3. There are currently 18 centrally assessed pipeline companies, whose property is classified as class 9 property.
4. Of these 18 companies, three companies pay oil and gas production taxes. Under HB 569, the property classification of oil and gas production companies moves from class 9 at 12%, to class 8 at 3%. All of the property of two companies would be classified as class 8 property, while only a portion of the value of the third would be classified as class 8 property. (See assumptions #1 and #4)

5. The oil and gas production property reported by centrally assessed pipeline companies that are not liable for production taxes would remain classified as class 9 with tax rate of 12%. (See technical note # 1)
6. In the past, DOR has relied on the reporting of companies as to what property is production and transmission, which may or may not be comparable to how the department would define the property in an appraisal of the property. For purposes of this fiscal note, it is assumed that the market value of gathering lines will not change as a result of being transferred from central to local assessment by this bill. (See technical concerns #2 and #3)
7. This bill has a retroactively applicable to tax years beginning after December 31, 2004, or tax year 2005 (FY 2006).
8. The total market value of affected pipeline property for tax year 2004 (FY 2005) is estimated to be $30,687,318. (See technical notes #1 through #4)
9. Class 9 property is projected to decline by -0.1% each year over the biennium. FY 2006 and FY 2007 market values are estimated using the forecasted annual growth rate of –0.1%.
10. Table 1 shows the proposals estimated fiscal impacts to the state general fund and the university 6 mill account.

TABLE 1. OIL & GAS PRODUCTION PROPERTY

Description	**Current Law**	**Under HB569**	**Fiscal Impact**
Tax Class	Class 9	Class 8	
Tax Year 2004 (FY 2005) Market Value	30,687,318	30,687,318	
Forecast Growth Rate	-0.1%	-0.1%	
FY 2006			
Description	**Current Law**	**Under HB569**	**Fiscal Impact**
Forecast Tax Year 2005 (FY 2006) Market Value	30,656,631	30,656,631	
Taxable Rate	12.0%	3.0%	
Taxable Value	3,678,796	919,699	(2,759,097)
General Fund Taxes (95.53 mills)	351,435	87,859	(263,576)
University 6 mills SSR	22,073	5,518	(16,555)
FY 2007			
Description	**Current Law**	**Under HB569**	**Fiscal Impact**
Forecast Tax Year 2006 (FY 2007) Market Value	30,625,974	30,625,974	
Taxable Rate	12.0%	3.0%	
Taxable Value	3,675,117	918,779	(2,756,338)
General Fund Taxes (95.53 mills)	351,084	87,771	(263,313)
University 6 mills SSR	22,051	5,513	(16,538)

11. As Table 1 shows, the proposal by reducing taxable values statewide would *reduce* general fund revenues by $263,576 ($2,756,338 x 95.53 mills) in FY2006, and $263,313 ($2,756,338 x 95.53 mills) in FY 2007. (See technical notes)
12. The university system 6 mill account would be *reduced* by $16,555 ($2,756,338 x 6 mills) in FY 2006, and $16,538 ($2,756,338 x 6 mills) in FY 2007.

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(continued)

Impact on Class 12 Property

13. All property moving into class 8 is considered commercial property, but under the bill is taxed at a lower tax rate. The new lower tax rate will reduce the taxable rate for class 12 property (railroad and airlines) – which is the average commercial tax rate statewide.
14. It is projected that change in taxable values associated with reclassifying oil and gas production property of producers will change the projected class 12 tax rate from 3.75% to 3.73% in FY 2006, and from 3.69% to 3.67% in FY 2007.
15. The table below shows the anticipated change in class 12 taxable value, and fiscal impacts to the general fund and the university 6 mill account.

TABLE 2. CHANGE IN CLASS 12 (Railroad and Airline)

FY 2006			
Description	**Current Law**	**Under SB519**	**Fiscal Impact**
Forecast Tax Year 2005 (FY 2006) Market Value	1,193,693,570	1,193,693,570	
Taxable Rate (forecast)	3.75%	3.73%	
Taxable Value (forecast)	44,763,509	44,524,770	(238,739)
General Fund Taxes (95.53 mills)	4,276,258	4,253,451	(22,807)
University 6 mills SSR	268,581	267,149	(1,432)
FY 2007			
Description	**Current Law**	**Under SB519**	**Fiscal Impact**
Forecast Tax Year 2006 (FY 2007) Market Value	1,204,436,813	1,204,436,813	
Taxable Rate (forecast)	3.69%	3.67%	
Taxable Value (forecast)	44,443,718	44,202,831	(240,887)
General Fund Taxes (95.53 mills)	4,245,708	4,222,696	(23,012)
University 6 mills SSR	266,662	265,217	(1,445)

16. Class 12 is projected to have a market value of $1.194 million and $1.204 million in FY 2006 and FY 2007 respectively. With the lower tax rates of 0.02% each year, the change in class 12 taxable value is estimated at approximately $238,739 in FY 2006, and $240,887 in FY 2007.
17. Due to the estimated change in class 12, the general fund would *decrease* by $23,012 ($238,739 x 95 mills) in FY 2006, and $23,012 ($240,887 x 95 mills) in FY 2007.
18. Due to the estimated change in class 12, the university 6 mill account would *decrease* by $1,432 ($238,739 x 6 mills) in FY 2006, and $1,445 ($238,739 x 6 mills) in FY 2007.
19. Department of Revenue does not anticipate any additional administrative costs under the provisions of the bill.

Office of Public Instruction

20. The reduction in property tax values from the proposal would impact the state's obligation to fund the guaranteed tax base aid for school districts and counties.
21. It is assumed that property taxable value changes occur evenly across the state.
22. Property tax values decrease by 0.1669% in FY 2006. There will be a one-time guaranteed tax base (GTB) cost spike. The guarantee level is determined by the prior year taxable values applied against current year taxable values. The higher guarantee level in FY 2005 will apply to the lower taxable values in FY 2006 and cause increased state contribution as districts levy more mills to compensate for the drop in taxable values.

23. The decreased cost for guaranteed tax base aid for the district general fund will be $71,709 in FY 2006. Countywide retirement GTB will decrease by $30,913 in FY 2006 based on a historical average of 27% of the costs paid for by the state and FY 2004 county levies equal to $68.6 million ($30,913 =0.1669% x $68.6 million local levies x 27%).

FISCAL IMPACT:

	FY 2006 Difference	FY 2007 Difference
Expenditures:		
Local Assistance (OPI)	$102,622	$0
Funding of Expenditures:		
General Fund (01)	$102,622	$0
Revenues:		
General Fund (01)	($286,383)	($286,325)
State Special Revenue (02)	($17,987)	($17,983)
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):		
General Fund (01)	($389,005)	($286,325)
State Special Revenue (02)	($17,987)	($17,983)

EFFECT ON COUNTY OR OTHER LOCAL REVENUES OR EXPENDITURES:

1. a. This bill would impact local governments and school districts due to the estimated loss in taxable value of $2,997,836 in FY 2006, and $2,997,225 in FY 2007. (See technical notes #1 through #4).
   b. The statewide average local mill levy for gathering lines of centrally assessed pipelines in tax year 2004 (FY 2005) is estimated at 343.44. Statewide mill levies have increased annually by 4.5 percent since FY 2001. Assuming growth of 4.5%, the average local mill levy for gathering lines of centrally assessed pipelines would be 349.49 (343.44 x 104.5%) in FY 2006, and 365.21 (349.49 x 104.5%).
   c. The associated revenue decrease to local governments and school districts under the proposal is estimated to be $1,047,713 ($2,997,836 x 349.49 mills) in FY 2006, and $1,094,617 ($2,997,225 x 365.21).
2. Under 15-10-420, MCA, county and city governments could float their mill levies to offset this property tax revenue loss. Since the amount of loss associated with this bill is significant, mill increases could be very large in some areas; this would shift the impacts onto other taxpayers. Since oil and gas property is localized in particular areas, the impacts also would be very specific to a limited number of taxing jurisdictions.
3. This bill would increase local school district levies. State guaranteed tax base (GTB) aid will partially offset the local mill increase in FY 2006, but after the one year these additional mills will be fully born by the district levies.

LONG-RANGE IMPACTS:

This bill will reduce general fund revenues in the future by approximately $286,000 per year.

TECHNICAL NOTES:

1. Under the proposal, in order to qualify for local assessment and the lower tax rate, a non-producer would only need to purchase a well and pay the oil and gas production taxes under Title 15, Chapter 36 MCA. If a company would receive a tax benefit under such a scenario, pipeline companies would likely make such a purchases. It is conceivable that all pipeline companies would buy a well and pay a small amount of production tax to receive the tax benefit. The fiscal note does not assume this scenario, under such a scenario; the fiscal impacts would *increase significantly*.
2. In the event that a centrally assessed company sells some of its pipeline property in Montana to a new purchaser, after the purchaser allocates the purchase price to assets in other states and to gas reserves acquired, they may report a cost for the Montana pipeline property that is considerably less. In a past instance, the amount of allocated value after the sale of one large pipeline was less than 10% of the cost that had been reported by the previous owner.
3. If the value of gathering lines decreases further under local assessment, the reductions in tax revenue could be considerably larger.
4. 15-23-101(2), MCA, as amended could be misconstrued to imply that no oil and gas production or gathering property is centrally assessed. If this happens, the gathering property of non-producers would be separately assessed in class 8 under 15-6-138(1)(n), MCA, the catchall for property not elsewhere described. In this case the fiscal impact would be the same as for the introduced version of this bill. The bill should provide clarification.
5. Most property taxes are paid in November and May of the fiscal year following assessment. However, under the provisions of 15-16-119, MCA, owners of personal property that is not-liened to real property pay property taxes 30-days after assessments are mailed. This means that instead of paying taxes in November and May of the following fiscal year, they will pay sometime before April in the current fiscal year. It is unknown if, or what proportion of the production property would be not-liened to real property. Under the proposal, if a production property is locally assessed and *considered* not-liened to real, tax payments would be due earlier in the year; this means that taxes would be collected on some property twice in the same fiscal year (taxes due from the prior tax year and taxes due for the current tax year). Because the amount of property that is not-liened to real property is unknown, and the proposal does not detail when such property would be taxed, the fiscal note does not consider this change in the timing of tax payments.
6. This bill does not define the term “transmission line”. This could be important if the intent of the bill is to clarify the law and reduce disputes between the taxpayer and the Department of Revenue.